

This letter discusses donor/donee situations and Service Occupation Tax. See 86 Ill. Adm. Code 150.305 and 35 ILCS 115/3. (This is a GIL).

November 28, 2005

Dear Xxxxx:

This letter is in response to your letter dated June 17, 2005, in which you request information. The Department issues two types of letter rulings. Private Letter Rulings ("PLRs") are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A PLR is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the PLR are correct and complete. Persons seeking PLRs must comply with the procedures for PLRs found in the Department's regulations at 2 Ill. Adm. Code 1200.110. The purpose of a General Information Letter ("GIL") is to direct taxpayers to Department regulations or other sources of information regarding the topic about which they have inquired. A GIL is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120. You may access our website at www.ILTAX.com to review regulations, letter rulings and other types of information relevant to your inquiry.

The nature of your inquiry and the information you have provided require that we respond with a GIL. In your letter you have stated and made inquiry as follows:

As a service to our franchisees located within your state, ABC respectfully requests a written determination as to the proper sales/use tax treatment of the following items sold to our franchisees.

ABC is responsible for developing the data, concepts or ideas to be marketed, completing an analysis of the available media and means to advertise, completing an analysis of the present and potential markets, studying the products/services to be promoted, placing the advertising in the media and creating the formulation of an advertising plan.

ABC creates the following advertising items: banners, posters, audio or visual commercials, brochures, catalogs, direct mail advertising materials, direct marketing materials, display signs, flyers and handouts, sales promotion materials and table tent. All of these items are then sent out to a third party to create or print the finished product. The third party then ships the finished product to ABC. In return, ABC sends these finished products to our franchisees:

Is the final exchange of the marketing materials between ABC and our franchisees a taxable transaction?

We would also be interested in knowing about other possible factors that may be considered in determining the taxability of these items.

If you have any questions, please give me a call.

DEPARTMENT'S RESPONSE

Without reviewing the Company's specific contractual obligations with its franchisees or with its third party vendors, and without the registration status of the servicemen involved, the Department is without sufficient information to provide you with a specific response. However, I hope the following information regarding donor/donee situations and Service Occupation Tax is helpful.

If the arrangement between a business and its franchisees is such that the business provides tangible personal property to the franchisee free-of-charge, then a donor/donee situation may exist. A donor who purchases tangible personal property and gives the tangible personal property to a donee makes a taxable use of the property when making the gift. See 86 Ill. Adm. Code 150.305(c). A donor owes Use Tax on the donor's cost price of the tangible personal property that is transferred. You may want to review Department letter rulings on our website regarding the delivery of printed material into this State. See for example, ST 04-0200-GIL.

However, if the business sells custom print tangible personal property to the franchisee, then the Service Occupation Tax may apply. The Service Occupation Tax is a tax imposed upon servicemen engaged in the business of making sales of service in this State, based on the tangible personal property transferred incident to sales of service. See 35 ILCS 115/3. Under Illinois tax law, the transfer of special order printing materials is a service transaction that may result in either Service Occupation Tax or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. For general information, see 86 Ill. Code 140.101 through 140.109 regarding sales of service and Service Occupation Tax.

A serviceman's liability may be calculated in one of four ways: 1. Separately stated selling price of tangible personal property transferred incident to service; 2. 50% of the serviceman's entire bill; 3. Service Occupation Tax on the serviceman's cost price if he is a registered de minimis serviceman; or, 4. Use Tax on the serviceman's cost price if he is a de minimis serviceman not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of the sale price of service. The tax is then calculated on the separately stated selling price of the tangible personal property transferred. If the servicemen do not separately state the selling price of the tangible personal property transferred, they must use 50% of the entire bill to the service customer as the tax base. Both of the above methods provide that in no event may the tax base be less than the serviceman's cost price of the tangible personal property transferred. See 86 Ill. Adm. Code 140.106. These methods result in the customer incurring a Service Use Tax liability. See 86 Ill. Adm. Code 160.101.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. See 86 Ill. Adm. Code 140.109. Servicemen may qualify as de minimis if they determine that the annual aggregate cost price of tangible personal property transferred incident to the sale of service is less than 35% of the total annual gross receipts from service transactions (75% in the case of pharmacists and

persons engaged in graphics arts production). Servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. Registered de minimis servicemen are authorized to pay Service Occupation Tax (which includes local taxes) based upon their cost price of tangible personal property transferred incident to the sale of service. Such servicemen should give suppliers resale certificates and remit Service Occupation Tax using the Service Occupation Tax rates for their locations. This method also results in the customer incurring a Service Use Tax liability.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Such de minimis servicemen handle their tax liability by paying Use Tax to their suppliers. If their suppliers are not registered to collect and remit tax, the servicemen must register, self-assess and remit Use Tax to the Department. The servicemen are considered to be the end-users of the tangible personal property transferred incident to service. Consequently, they are not authorized to collect a "tax" from the service customers. See 86 Ill. Adm. Code 140.108. Under this method the customer incurs no Service Tax liability.

If a business takes orders for custom print tangible personal property and then farms these orders out to special order printers who actually do the work, then the business is functioning as a primary serviceman in a multi-service situation. The taxability of a primary serviceman in a multi-service situation is set out in 86 Ill. Adm. Code 140.145.

I hope this information is helpful. If you require additional information, please visit our website at www.ILTAX.com or contact the Department's Taxpayer Information Division at (217) 782-3336. If you are not under audit and you wish to obtain a binding PLR regarding your factual situation, please submit a request conforming to the requirements of 2 Ill. Adm. Code 1200.110 (b).

Very truly yours,

Martha P. Mote
Associate Counsel

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